
**AUDIT OF REVENUE
MANAGEMENT PRACTICES
AT THE KENTUCKY HORSE PARK**

JUNE 1997



**EDWARD B. HATCHETT, JR.
AUDITOR OF PUBLIC ACCOUNTS**



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June 27, 1997

To the People of Kentucky
The Honorable Paul E. Patton, Governor
Ann R. Latta, Secretary of the Tourism Development Cabinet
Cornelia W. Bonnie, Chair of the Kentucky Horse Park Commission
John Nicholson, Executive Director of the Kentucky Horse Park

Re: Performance Audit of the Kentucky Horse Park

Ladies and Gentlemen:

We present our report on revenue management practices of the Kentucky Horse Park (Park). Our report examines Park management's maximizing of revenue from Park activities for the purposes of 1) generating funds for continuing maintenance and investment in the Park, and 2) minimizing taxpayer subsidies in the form of General Fund appropriations covering operations and debt service of the Park.

Since 1978, when the Park hosted its first major event, the Kentucky Horse Park Commission has succeeded in expanding Park exhibits and attracting special events to the Park. Several events have been turned away this year because of the full calendar of 67 events which are scheduled for the 1997 tourist season. While the Park still requires General Fund appropriations in order to meet its operating expenses, invest in new facilities, and increase its marketing efforts – a full assessment of the Kentucky Horse Park must consider the large economic impact it provides and such intangibles as the enhancement of the state's image. We believe that the findings and recommendations contained herein will help improve Park operations.

Our report shows that the Park does not have the capability to adequately track costs by activity, facility, or event. Therefore, the Park cannot determine what expenses it incurs for each activity or event. By improving its cost accounting ability, the Park can take advantage of previously lost opportunities to bill for services and make informed management decisions regarding options for increasing revenue. We also noted that Park management can improve its monitoring of contractual arrangements. We recommend that Park management maintain written contracts governing all transactions between the Park and other parties, including the Kentucky Horse Park Foundation.

The Secretary of the Tourism Development Cabinet and Park management have concurred with our recommendations. Park management has already taken steps to implement recommendation 1.5 regarding the maintenance of contracts, therefore this recommendation is considered closed. The remaining recommendations will be considered closed once the respective offices have advised us that the recommendations have been implemented.

Respectfully submitted,

Edward B. Hatchett, Jr.

Executive Summary

While the Kentucky Horse Park requires General Fund appropriations, studies have shown that it has produced a significant economic benefit for the state. Any assessment of the Park must consider the full value of the Park, including such intangibles as the enhancement of the state's image. Nonetheless, sound public stewardship dictates that the Park maximize revenues, while serving the objectives for which it was created.

Our audit found that management of the Kentucky Horse Park relies heavily upon significant and increasing General Fund support and that management does not maximize the Park's ability to generate funds. We concluded that the Park should consider billing and collecting the full costs of all services, including:

- over \$103,500 in maintenance and support for special events;
- \$22,664 in waste water treatment services the Park provides to others;
- security, garbage collection, and groundskeeping fees from lessees;
- utilities used by special events and other tenants, and
- security deposits from event sponsors.

We also found that some events are given discounts on published prices, while other events are turned away. One reason park management cannot ensure that revenue has been maximized is that the Park lacks a system to collect adequate cost information related to each activity or event at the Park, and thus cannot rationally choose among the events.

We encourage the Park to review its business focus, taking advantage of existing revenue sources and properly allocating costs. By improving its ability to generate revenue, the Park can ensure that it does not require greater taxpayer subsidy than is necessary. We also believe that greater attention to Park budgeting and spending by the Tourism Development Cabinet will help assure a more business-like management approach at the Park with regard to revenue generation. We are encouraged by ongoing efforts of the Commission and Foundation to develop options for increasing Park revenue.

The following contracting weaknesses at the Park should also be addressed:

- Several agreements with other parties are not governed by written contracts;
- Contracts are not managed by a single Park office;
- Lease agreements are not routinely monitored, resulting in revenue not being collected;
- Not all business arrangements with the Kentucky Horse Park Foundation are financially segregated and contractually controlled; and
- Contractual agreements and the revenue generated by the Park receive limited oversight by the Tourism Development Cabinet.

As part of our analysis we noted that:

- The Park has received between \$2,067,400 and \$2,466,000 each year for the past 5 years from the General Fund for debt service and operating costs;
- KRS 148.320 requires that revenue from the Park be used to defray operating and debt service costs, as well as generate funds for maintenance, investment, and marketing efforts; and
- The Park is requesting higher levels of General Fund support to fund construction and maintenance.

We recommend that:

- The Secretary of the Tourism Development Cabinet or a designee annually review and approve the Park's fee structure and review and offer comments on the annual revenue and expenditure budget;
- The Kentucky Horse Park Commission establish annual performance objectives for the Park and the Executive Director; and
- The Executive Director of the Park establish a cost accounting system which allocates costs to individual facilities, activities, and events, and identifies the incurred operating gain or loss for each event.

A more detailed listing of our recommendations may be found on page 19 of this report.

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Introduction

Background

From the initial purchase in 1972, the Kentucky Horse Park has evolved from the privately-owned Walnut Hall Stud farm into a living museum of Kentucky's horse industry. The facility hosts a number of attractions within its 1,032 acres. Equine and non-equine events fill the calendar of the Park during its open season, attracting tourists and exhibitors to the Commonwealth and creating a sizable economic impact in the surrounding communities. Over time, the management structure of the Park has evolved as well, reflecting the interests of succeeding administrations. Outside organizations, most notably the Kentucky Horse Park Foundation, have made significant contributions to the Park and its facilities.

Total land costs for the Park amounted to \$2,953,750, of which \$1,250,000 was provided by a Federal Grant from the Bureau of Recreation. Before the Park opened to visitors in September, 1978, another \$32,000,000 in state funds had been spent developing Park facilities, including (1) a seven acre lake and resort campground; (2) 27 miles of fencing; (3) facilities for steeplechase, dressage, and stadium jumping; (4) two theaters; (5) a museum and restaurant; and (6) the creation of an exit for the Horse Park off I-75.

Park Management Structure Has Changed On Several Occasions

In 1979, the Legislature shifted oversight responsibility for the Kentucky Horse Park from the Department of Parks and created the Kentucky Horse Park Management Board, similar to the State Fair Board, to manage the Park. In 1980, Governor Brown restructured the Board, reducing it from 19 to 7 members. The current management structure, established in 1985 by Governor Collins, replaced the Kentucky Horse Park Management Board with the Kentucky Horse Park Commission. According to current Park management, it was after the formation of the Commission that events and attractions of the Park increased, leading to the currently full calendar of tourist season events at the Park.

The Kentucky Horse Park Commission is a 17 member body which functions as a separate administrative unit of state government, attached to the Tourism Development Cabinet for administrative purposes. Fifteen members of the Commission are appointed by the Governor. The remaining two commission members, the Secretary of the Tourism Development Cabinet and the Secretary of the Economic Development Cabinet, serve as ex officio members, with the same voting rights as any other member of the Commission.

The Horse Park Commission was granted authority and control over Park property by statute, and was directed to "... promote the progress of the state and stimulate public interest in the advancement and development of the state by providing the facilities of the State Horse Park for exhibitionary, competitive, and other events relative to various aspects of the horse industry and other functions calculated to advance and enhance the tourist industry, economy, entertainment, cultural, and educational interests of the public." It is also the responsibility of the Horse Park Commission to select an Executive Director, whose function is to serve as administrative head of the Kentucky Horse Park.

Foundation Support Has Been Beneficial

In 1985, the Kentucky Horse Park Education Foundation, Inc. was formed. This private, not-for-profit corporation – which is now known as the Kentucky Horse Park Foundation – was organized to provide financial and other support exclusively for the Kentucky Horse Park. A recent Foundation publication states that the organization, since its inception, has raised over \$6,000,000 in cash and kind, including funding or donations for horses, equipment, two fifty-stall barns, creation of six polo fields, and other items for the Kentucky Horse Park. Many of these facility improvements at the Park have contributed to the ability of Park management to attract large equine special events to the Park. Corporate sponsorship included in the above amount provided several of the vehicles used at the Park, as well as other equipment. All but one member of the Kentucky Horse Park Commission also serve on the Kentucky Horse Park Foundation Board.

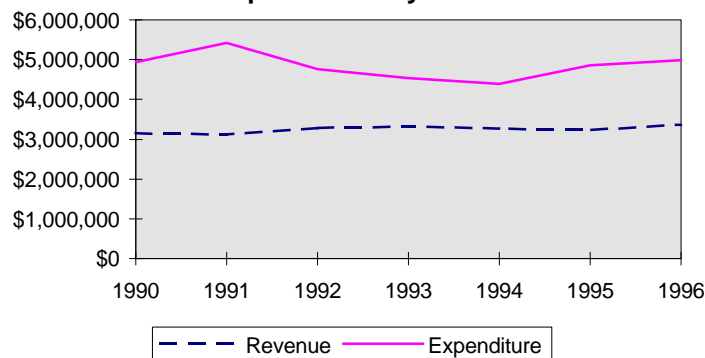
The Park Has Made a Substantial Economic Impact

According to the Kentucky Department of Travel Development, the Kentucky Horse Park has made a substantial contribution to the state's economy. The Department estimated the economic impact of the Kentucky Horse Park at nearly \$95,000,000 in 1995 alone. This impact is derived from hotel, restaurant, and additional tourist activities outside the Park. Additionally, the Department of Travel Development estimated that tourists generated over \$10,000,000 in state and local taxes in 1995 as a result of activities related to the Horse Park¹. From 1984 to 1995, spending by tourists related directly to the Kentucky Horse Park increased by 442 percent, far outpacing the tourism industry's state-wide increase of 152 percent.

Operating Losses Have Required General Fund Support

Despite the economic impact the Park provides, paid admission to the Kentucky Horse Park has been generally declining since 1988. Through increases in general admission fees, revenue generated by the Park (as shown in figure 1) has been virtually unchanged since 1990.

Figure 1: Kentucky Horse Park Revenue and Expenditures by Fiscal Year



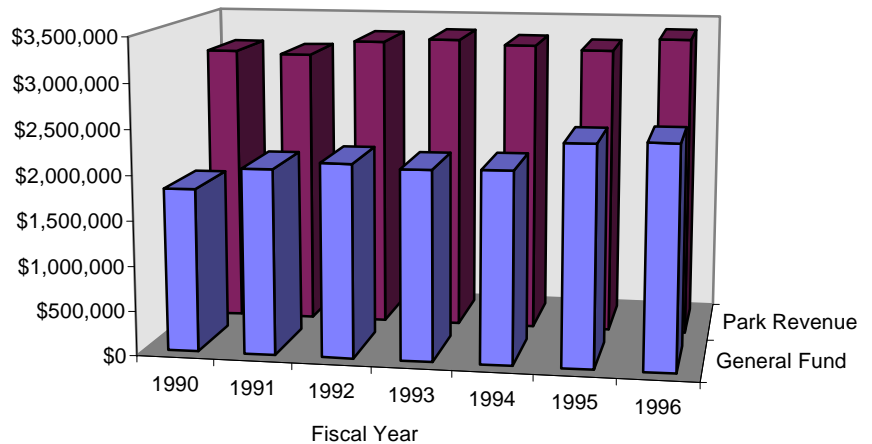
Source: APA and Independent Audit Reports and Tourism Development Cabinet Budget

This lack of revenue growth has contributed to a steady decline in the ability of the

¹ Given the scope of our audit, we neither verified the accuracy of the Kentucky Department of Travel Development estimate of the Kentucky Horse Park's economic impact nor the methodology used in arriving at this estimate.

Park to cover its operating expenses and debt service cost. Consequently, the Park's General Fund Appropriation as a percentage of Park Revenue has risen from 58% in 1990 to 73% in 1996. Without additional revenue, this increasing dependence on General Fund support, as illustrated in figure 2, will continue.

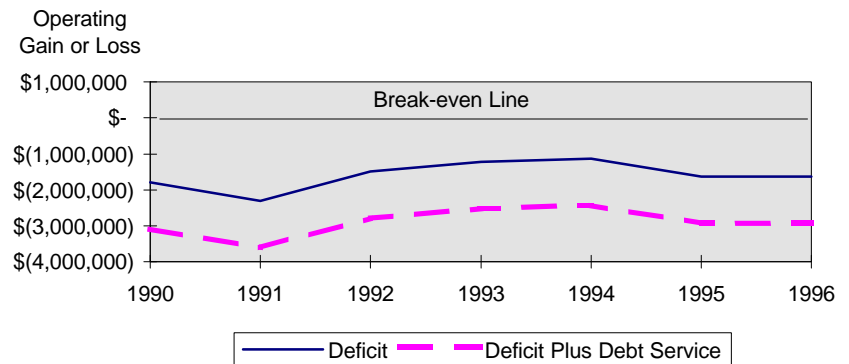
Figure 2: Comparison of Kentucky Horse Park General Fund Appropriation to Park Revenue



Source: APA and Independent Audit Reports and Tourism Development Cabinet Budget

The Park's operating loss (revenues less expenditures) as compared to its break-even point is illustrated in Figure 3 below. The Park relies on General Fund support in order to cover those operating costs which exceed the revenue generated by the Park. The addition of the Park's debt service repayment further increases the reliance on the General Fund.

Figure 3: Kentucky Horse Park Break-even Analysis



Source: APA and Independent Audit Reports and Tourism Development Cabinet Budget

Audit Objective

Given the changes to the Park's management structure over the years and the potential for an increasing dependence on General Fund support, our audit was designed to answer the following question:

Does Kentucky Horse Park Management Ensure That Revenue Opportunities Appropriately Defray Park Expenses?

In order to answer this question, we reviewed the enabling legislation of the Park and other relevant statutes. We conducted interviews with Park management and Cabinet for Tourism Development officials. We also reviewed financial information and contractual documents on the premises of the Kentucky Horse Park.

Our audit was conducted in accordance with generally accepted governmental auditing standards. Appendix I contains the scope and methodology of our audit.

Does Kentucky Horse Park Management Ensure That Revenue Opportunities Appropriately Defray Park Expenses?

Summary

While management of the Kentucky Horse Park has created an acclaimed attraction for showcasing the horse industry, hosting world class equine events, attracting tourism, and creating a positive economic impact on the community, revenue opportunities which could increase the Park's potential are being lost due to conflicting Park objectives and inequity in the allocation of Park operating costs. Because the Park is subsidized by taxpayers, we believe operations of the Park should be managed efficiently and costs should be borne equitably, through appropriate fees and charges, by the various users of Park facilities. Although the Park may not be expected to earn a profit or completely end its need for General Fund support, attention to revenue generation is needed in order to ensure that the original mandate of the Park "...for recreational and educational purposes, in commemoration of the influence of the thoroughbred horse industry on the history and traditions of the Commonwealth" is fulfilled. Targeted oversight by a state cabinet will ensure that the Park will not require greater than necessary support from the state, or be forced to curtail its world-renowned activities.

Management of the Park Has Undertaken Several Initiatives to Expand Activities and Improve Park Operations

The Kentucky Horse Park markets itself to several different user groups throughout the year. Marketing efforts target several broad market segments including tour and motor coach operators, meeting and convention organizers, and the general public. The Park is a working horse farm with over 100 horses which must be fed and groomed daily. A Parade of Breeds and other horse shows are conducted each day by Park staff. In order to draw more tourists, the Park operates a campground, hosts a visitor information center throughout the year, and develops a calendar of equine and non-equine special events. For example, Old Kentucky Nights, one of the non-equine special events, has brought groups from area conventions and motor coach tours to the Park after normal operating hours, thus increasing the opportunities to generate revenue. The Park's peak tourist season for 1997 – April 1 through October 31 – has been fully booked for events (See table 1 on the next page). The Park's 95 permanent part-time and full-time staff often work weekends and evenings during the tourist season, sometimes rotating shifts in order to handle the wide variety of events which bring patrons to the Park each year.

We remain concerned, however, that despite this dedication and innovation, Park revenue growth remains negligible.

Kentucky Horse Park management has developed a Master Plan, calling for further investments in the Park through the year 2000. Park officials hope a newly-signed catering agreement will increase revenue for the Park by establishing a commission payable not only for catering events but also for the rental of tents, chairs, tables, and other items. Additionally, plans call for the development of an unique virtual reality exhibit at the Park's museum. We are encouraged by the dedication of the Park's staff and the innovation involved in developing some of the plans underway for the Park. We remain concerned, however, that despite this dedication and innovation, Park revenue growth remains negligible.

**Does Kentucky Horse Park Management Ensure That Revenue Opportunities
Appropriately Defray Park Expenses?**

Table 1: 1997 Events At The Kentucky Horse Park

Horse Shows

- Champagne Run Moonlight Ride Hunter/Jumper Show
- Iroquois Hunt Point to Point
- Kentucky Arabian Horse Association Show
- Ha' Penny Horse Trials - Spring & Fall
- Spring Horse Affair Fun Show
- Mid-South Pony Club Games Rally
- Rolex Kentucky 3-Day Event
- Kentucky Spring Premier Saddlebred Show
- Kentucky Spring Horse Show
- Kentucky Spring Classic
- Kentucky Dressage Association Annual Show
- High Hope Steeplechase
- Bluegrass Horse Trials
- 17th Annual Egyptian Event
- Mid-South Regional Pony Club
- Paso Fino Festival of the Bluegrass
- Region 14 Silverama Arabian Show
- Robert Murphy Hunter/Jumper Show
- U.S. Team Roping Championship Eastern Finals
- Mid-America Miniature Horse Association Julep Cup
- Champagne Run Horse Trials
- Wild Horse and Burro Adoption and Expo
- Kentucky Horse Fair
- Shetland Pony Show
- County Fair Circuit Harness Racing
- Eastern Summit Paint Horse Show
- Bluegrass Festival Hunter/Jumper Show
- Kentucky Hunter/Jumper Association Annual Show
- All-Arabian Combined Classic I & II
- 13th Annual Mounted Police Colloquium
- 9th Annual Rocky Mountain Horse Show
- Kentucky National Hunter/Jumper Show

Horse Shows

- Dressage at the Horse Park
- Kentucky Quarter Horse Futurities
- Jump Start Horse Trials
- Kentucky Fall Classic Saddlebred Show
- M.S.C.T.D.A. Team Challenge Horse Trials
- Sheiks and Shrieks Arabian Fun Show

Dog Shows

- Lexington Kennel Club Julep Cup Show
- Mid-America Foxhound Show
- Saluki Club of America National Specialty Dog Show
- Bluegrass Classic Dog Show

Concerts

- Festival of the Bluegrass
- B.B. King

Other Events

- Boy Scout World
- Kentucky Heritage Quilt Society Annual Exhibition
- Kentucky High School Rodeo Association Annual Rodeo
- Week-end of Driving
- Breyerfest
- All Kentucky Ag Expo
- Southern Lights
- Halloween Parade of Breeds
- High School Cross Country Track Meet
- Kentucky Kickers Soccer
- Polo

**Park Management Needs
to Review Its Business
Focus Regarding
Revenue Generation**

As a public enterprise whose main sources of revenue consist of public admission fees and General Fund support, we believe sound public stewardship dictates that the Kentucky Horse Park maximize the fees it collects while serving the goals and objectives for which the Park was created. The Legislature intended that the Park use all available revenue to support and invest in the operations of the Park and to ensure that any General Fund support be kept to a minimum. KRS 148.320 in part states:

All revenues derived by the commission from the use of properties and facilities under its custody and control shall be used exclusively for the purpose of defraying the expenses of the commission, the cost of the management and operation of such properties and facilities, the payment of interest and principal upon any indebtedness incurred by the commission for such properties and facilities, the creation of adequate reserves for the repair and replacement thereof and for the financing of further extensions, improvements, and additions thereto. Included in the cost of operation may be such promotional activities as the commission may determine upon as calculated to stimulate and increase the use and the revenues of such facilities, and to increase and stimulate the interest and usefulness of the State Horse Park.

In the opinion of the Attorney General (80-399), this statute intends that the Park be independent and self-sufficient. While we do not believe self-sufficiency is a goal that will be obtained in the immediate future, the goal of “defraying the expenses of” the Park seems quite clear. As we noted earlier, the Kentucky Horse Park is attached to the Tourism Development Cabinet for administrative purposes and functions as a budget unit of the Cabinet. The Park’s budget is submitted to the Secretary of Tourism Development, who can approve, disapprove, modify, or otherwise amend the budget request of any budgetary unit or administrative body within the Cabinet. We believe it is incumbent upon the Secretary of the Tourism Development Cabinet to closely monitor the revenues and expenditures, fee structure, contracts, and other activities of the Park involving the collection and expenditure of state funds.

KRS 148.280 (1)(c) also states that one of the functions of the Kentucky Horse Park Commission shall be to “promote the progress of the state and stimulate public interest in the advancement and development of the state by providing the facilities of the State Horse Park for exhibitionary, competitive, and other events relative to various aspects of the horse industry and other functions calculated to advance and enhance the tourist industry, economy, entertainment, cultural, and educational interests of the public”. The Kentucky Horse Park can accomplish this mission only if it has the necessary financial resources to market the Park, invest in new facilities, and improve the attractions and exhibits on the Park grounds as detailed in the Park’s Master Plan. The Park should not rely on General Fund support to provide these resources unless it has first exhausted all possible options for generating revenue on its own to fund these investments.

Our audit determined that the Kentucky Horse Park Commission and management need to review their business management focus with regard to maximizing revenue and equitably distributing the costs of running the Park to its many users. While general admission fees have increased steadily, stall rental fees have not risen as fast even though the Park's full schedule means that several hundred thousand dollars in events for 1997 have been turned away. Improvements in the management of event contracts and leases will also increase opportunities for revenue generation.

Opportunities to Recover Costs and Increase Revenue Have Been Underutilized

Ideally, revenues should cover operating costs and provide a reserve for investment in buildings, equipment and other capital improvements. At the same time, fees and charges should not exceed what potential customers are willing to pay to visit an attraction like the Park, or to use facilities like those available at the Park. While the Park has surveyed fees at other similar facilities, we believe the Park can improve its analysis in order to determine whether the Park is maximizing revenue from fees and charges as well as pursue revenue due it under existing arrangements. Specific opportunities to increase revenue and recover costs include the following:

Waste Water Treatment Facility - While the Kentucky Horse Park's waste water treatment facility receives roughly \$10,000 per year from properties which make use of the facility, the Park does not bill the full cost of sewer services to these entities. These properties include private and university organizations (the Asphalt Research Center, Council of State Governments, Energy Center, Spindletop Hall, and the University of Kentucky Geological Survey Building) as well as other state government facilities (the Finance Cabinet Office Building and the Finance Cabinet Office and Storage Building).

In the past year the Kentucky Horse Park Commission, in consultation with the Finance and Administration Cabinet and Lexington Fayette Urban County Government, has discussed various options for transferring responsibility of the facility and/or increasing user fees. We believe an appropriate fee structure should be established immediately so that private organizations do not receive free or subsidized services at taxpayer expense. Finalizing the responsibility for maintaining the facility and establishing the appropriate user fees will require coordination between the Park, the Public Service Commission, and the Finance and Administration Cabinet.

We contacted the Public Service Commission (PSC) to determine what options the Park could undertake to increase billings. A representative of the PSC stated that the PSC had to approve the fees set by the Park and – prior to our contact – was not aware that the Park maintained a treatment facility. According to the representative, the Park may charge an amount necessary to recover the costs associated with the treatment of the user facilities' waste water. An analysis conducted by Park personnel at the request of the Kentucky Horse Park Commission and our audit revealed that, in calendar year 1996, the Park could have billed an additional \$22,664 in order to defray the cost of the waste water treatment. Furthermore, this analysis underestimates the true cost of operating the waste water treatment facility

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because it does not include long-term costs such as depreciation and interest on debt for the facility. As a result of our discussions, Park management has contacted the PSC and requested guidance on the establishment of such fees.

We believe it is important that the Park receive an adequate fee for the services it provides in order to defray the costs of maintaining and updating its aging waste water treatment facility. Any future expansion of the sewage system should also consider the costs associated with expanding this system. According to Park managers, the system – although exceeding Kentucky Division of Water treatment standards – was designed without public service in mind and is already overextended and in need of repair.

Security Deposits - Event organizers are allowed free use of office space in the Park during the course of their events. Park management told us the office space is sometimes damaged during the events. However, no security deposit is collected to cover the cost of repair, nor are event organizers billed for the damages. Procedures should be developed to protect the Park from having to pay for repairs and extensive clean-up to the office space.

Major Events - In 1995 and again in 1996, Park management did not adequately plan for the traffic congestion caused by the staging of a concert event at the Park. In both instances, police informed Park officials that they must clear the roadways because traffic was backing up onto Interstate 75. As a result, Park officials opened the gates to the Park, and were thereby unable to collect the \$2.00 per car parking fee from a portion of the participants (8,821 attended in 1996.) We were unable to determine the amount of parking fees forgone by the Park, although the Park did collect \$5,225 in catering commission and \$1,881 in rental fees for the 1996 event.

Commission Relations With Outside Entities Need Review and Oversight

The Kentucky Horse Park Commission, as an agency of state government, and Park management are responsible for the policies and procedures regarding contractual arrangements at the Park. Our audit identified instances where contractual agreements were absent or not enforced.

Southern Lights - One particular example of the absence of contractual agreements involves the Kentucky Horse Park and the Kentucky Horse Park Foundation. In 1989, a management and accountability study of the Kentucky Horse Park by the Greater Lexington Chamber of Commerce, Committee for Progress and Efficiency in Lexington (ComPEL)² recommended that, “The Commission, the Kentucky Horse Park staff, and the Foundation’s Board of Directors should continue their current efforts to totally segregate fiscal operations of the Horse Park and the Foundation.” We believe that segregation of operations should require contracts and documentation regarding all Foundation hosted events and transfers of assets.

² Conducted by the Lexington Chamber of Commerce, the ComPEL III study looked at operations of the Park in 1989. See Appendix II for a complete listing of the ComPEL III recommendations.

Does Kentucky Horse Park Management Ensure That Revenue Opportunities Appropriately Defray Park Expenses?

In 1994, the Kentucky Horse Park Foundation and Lexington Herald Leader, Inc., entered into a joint-venture agreement to create an annual Christmas light show called Southern Lights, which was to be held on Kentucky Horse Park property. Subsequently, the Park entered into a rental agreement with the joint-venture for the 1994 Southern Lights show. Although there has been no formal contract since 1994 between the Foundation, Lexington Herald Leader, Inc., and the Commonwealth of Kentucky – the Horse Park bears the costs of labor and electricity, as well as the responsibility for making the facilities of the Park, including the Visitor Information Center and Museum, available throughout the event.

The Horse Park Foundation agreed to loan the joint-venture the funds necessary to purchase the lights for the event, and Lexington Herald Leader, Inc. agreed to provide personnel to produce local advertising and promotion for the show. The Park forgoes its normal parking fee of \$2 and its general admission charge of \$7.50 per person and instead receives a portion of the Southern Lights admission fee that is charged per vehicle for entrance to the Park. The Park does, however, benefit from the ability to attract visitors to the facility in the winter, a traditionally slow period for the Park. In 1996, an estimated 94,743 people attended Southern Lights in 22,495 vehicles. Additional revenues generated by gift shop and restaurant sales during Southern Lights for 1995 and 1996 were estimated by Park management to total \$6,149 and \$8,455, respectively.

Although the Park has no cost accounting system with which to determine what portion of electric, labor, museum, security, and other costs are attributable to the event, we estimate that it costs the Kentucky Horse Park over \$34,000 to host the Foundation's 1996 Southern Lights event. This estimate does not include the labor costs involved in tearing the exhibit down and storing the lights throughout the year. If the Park had received only the minimal \$2.00 it normally charges for parking from each vehicle visiting the 1996 Southern Lights exhibit – while still foregoing its \$7.50 admission fee – the Park would have received \$44,990 from the 1996 Southern Lights event. Of the total \$205,452 of revenue generated by Southern Lights direct admissions during this time, however, the Horse Park received only \$38,198 while the Horse Park Foundation/Herald Leader Joint Venture received the remaining \$167,254. Table 2 summarizes the admissions revenue sharing for Southern Lights for 1995 and 1996.

Table 2: **Southern Lights Revenue Sharing of Direct Admissions**

Calendar Year	Total Revenue	Southern Lights Joint Venture Share	Horse Park Share
1995	\$214,150	\$188,221	\$25,929
1996	\$205,452	\$167,254	\$38,198

Source: KHP Financial Summary Information

While the Kentucky Horse Park Foundation provides numerous benefits to the Park,

Does Kentucky Horse Park Management Ensure That Revenue Opportunities Appropriately Defray Park Expenses?

While the Foundation expects to make donations which exceed any revenue forgone by the Park, we are concerned that the Kentucky Horse Park lacks adequate contractual controls over the event.

the Foundation, as previously noted, is not an agency of state government. The Kentucky Horse Park Commission, as the party responsible for management of the Park, should ensure that whenever possible all Park users are charged rates appropriate to cover Park expenses, and minimize operating losses and General Fund support. While the Foundation expects to make donations which exceed any revenue forgone by the Park, we are concerned that the Kentucky Horse Park lacks adequate contractual controls over the event. Given that administration of the event is largely the responsibility of management and staff of the Park, future arrangements with the joint venture should consider compensation to defray the costs incurred by the Park in hosting the Southern Lights display. Other difficulties with the Park's contracting practices are noted below.

Office Leases - Of the business arrangements which were contractually controlled, we noted that the Park was not collecting fees from a contract between the Park and an organization renting space from the Park. This contract stipulated monthly fees for security and garbage services, sewer services, and grounds keeping services. As of January 1997, however, no fees had been collected, although the contract had been signed in June of 1991. This omission resulted in \$3,300 of lost revenue from uncollected fees for security and garbage collection since the contract's inception. We did not estimate revenue which would have been generated by the sewer fee because that amount is based on usage, and building sewer usage has not been monitored.

The Kentucky Horse Park, therefore, has no way of selecting the most economical mix of events among the many competing for the Park's facilities.

Contract Management - Our review of the Kentucky Horse Park's contracting procedures demonstrated that the Park has no systematic method of comparing the payments received from an event to the costs associated with hosting the event. As we noted earlier, the Park calendar is filled by special events, and business is being turned away. Without the ability to analyze the costs and benefits of each event, the Park has no way of rationally determining which events create an overall benefit for the Park and which events create an overall cost to the Park. The Kentucky Horse Park, therefore, has no way of selecting the most economical mix of events among the many competing for the Park's facilities.

Equitable Rate Setting Should Maximize User Fees

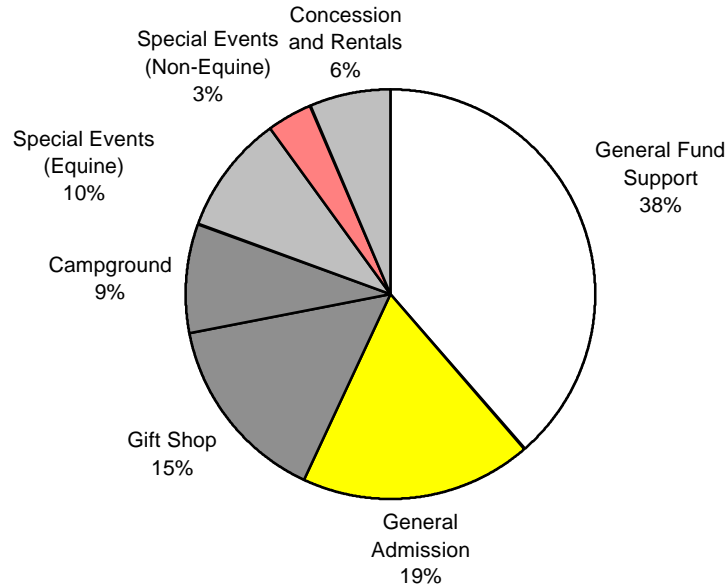
All users of the Park should be charged a price for use of Park facilities which approximates the maximum fee the market will bear. As shown in the figure 4 below, the state's General Fund and the Park's general admission ticket sales create the majority of Park revenue. General admission ticket sales allow tourists to visit the Horse Park Museum, Visitor Information Center, and other attractions at the Park. Special event revenue is derived primarily from contractual arrangements with event organizers.

In order to bolster revenues, the Commission has steadily increased the general admission price. Meanwhile, the number of paid general admission sales has generally declined over the past few years. The extent to which the increases in price will continue to erode attendance is unknown, but certainly remains a factor that must be weighed when pricing decisions are made at the Park. On the other hand, attendance at equine and non-equine special events has risen consistently over the

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past few years (see table 3 below).

**Figure 4: Fiscal Year 1996
Kentucky Horse Park Revenue Sources**



Source: KHP Financial Statements

Table 3: Change in Attendance by Market Segment from 1992 to 1996

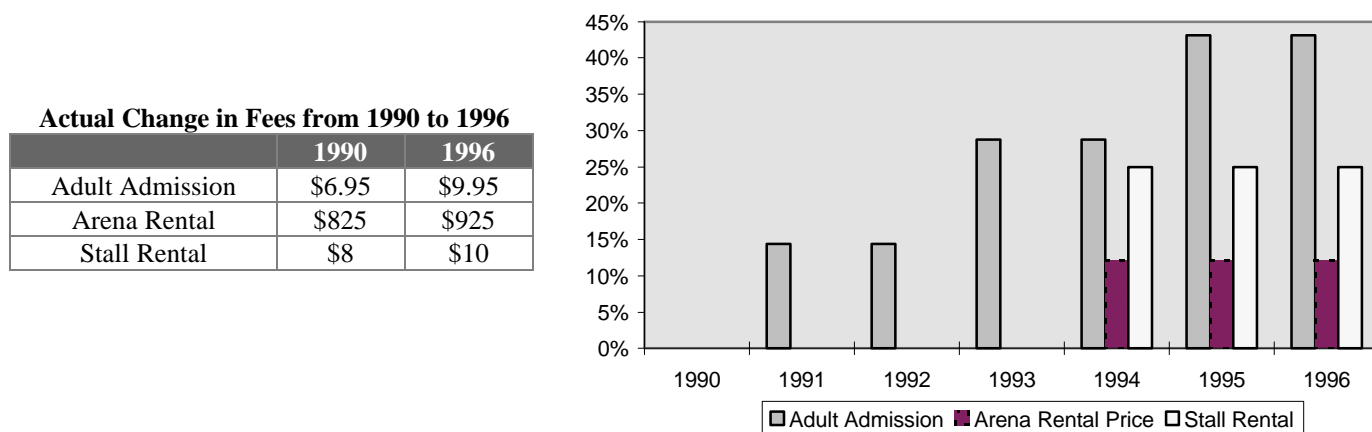
	General Admission		Special Event (Equine)		Special Event (Non-Equine)	
	1992	1996	1992	1996	1992	1996
Attendance	136,054	98,642	197,717	224,580	55,376	107,898
Percent Change in Attendance	-27%		14%		95%	

Source: KHP Fiscal Year 1996 Financial Statements

Given current trends, the Park must capitalize on the increasing special event markets if overall Park revenue is to at least hold constant. Without the benefit of more extensive analysis of costs associated with hosting these events and in-depth marketing studies, the Park has chosen not to raise facility rental and stall fees. Park management has based their pricing decision on an analysis of what other venues in surrounding states are charging. (Figure 5 compares the percentage increase in fees for adult admission, arena and stall rental since 1990.)

Does Kentucky Horse Park Management Ensure That Revenue Opportunities Appropriately Defray Park Expenses?

Figure 5: Cumulative Percent Increase In Fees Since 1990



Source: KHP Fiscal Year 1996 Financial Statements
(From 1990 to 1993, there was no change in Arena or stall rental prices.)

Without additional analysis, Kentucky Horse Park officials may be requiring the general populace to bear the majority of the costs at the Park through General Fund support and increases in general admission prices, instead of special event organizers. While subsidizing some events through general admission prices may be appropriate, taxpayers cannot be protected when subsidies are not identified, quantified, and appropriately limited. It may not be feasible for the Park to make a profit, but there are steps managers can take to ensure that everyone who uses the Park pays a fair market attendance fee. We believe effective management can minimize the cost to the Commonwealth of operating the Park while ensuring that the original goals and objectives of the Park are achieved. We found the following arrangements which Park management should review to ensure that revenue has been maximized:

Establishment of Stall Rates - When a special event involving horses is scheduled at the Park, the Park rents the stalls to the event organizer. The event organizer then rents the stalls to the event participants. We obtained entry forms for some of the equine-related special events held at the Park during 1996. While the Park received \$10.00 per stall night during 1996, the average amount the event promoters received for the shows we examined was \$20.00 per stall night. This amount does not include the amount the promoters charge for participants' entry fees, or the cost of feed and bedding.

Our audit revealed that the Commission declined to approve a \$3.30 increase in stall rental rates as requested by Park management in June of 1996 to defray the cost of disposing of horse waste and soiled wood chip bedding. The Commission instead approved, in December 1996, a \$1.00 increase per stall night. Horse owners had

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requested the more expensive wood chip bedding, as opposed to straw. Wood chip bedding, however, cannot simply be spread across the fields to dispose of it. Due to new environmental regulations, the soiled bedding must now be removed from the Park for disposal. Kentucky Horse Park management determined the soiled bedding could be composted at a nearby facility, but the waste must first be collected and then hauled away.

The cost to purchase the additional equipment and provide the labor to collect and haul the waste led to the proposal of the additional \$3.30 per stall night rate request. Instead, with the \$1.00 per stall night increase included, the Kentucky Horse Park now rents horse stalls at the rate of \$11.00 per night. During the 1996 season, the Horse Park rented out approximately 45,000 stall nights. If the Park rents out the same number of stall nights in 1997, the additional \$2.30 per night requested but not approved, would result in an additional \$103,500 for the Park to defray the cost of waste disposal. The table below projects the bedding removal cost that must be absorbed by the Park through the next three fiscal years.

Table 4: **Projected Additional Bedding Disposal Costs**

	Projected Stall Nights	Projected Disposal Cost	Revenue From \$1 Per Stall Night Increase	Disposal Cost Not Defrayed
1997-1998	37,132	\$100,955	\$37,132	\$63,823
1998-1999	38,245	\$109,183	\$38,245	\$70,938
1999-2000	39,393	\$118,081	\$39,393	\$78,688
Total Projected Cost Through Fiscal Year 2000				\$213,449

Source: KHP Management Analysis

Water Costs - Water usage may vary widely among the variety of events scheduled at the Park. However, because the Park does not routinely monitor water usage, the Park cannot equitably distribute the costs among the events. Park staff estimated that one recent horse show used an excessive amount of water during the course of a weekend event while the facilities rental received was only \$2,550 (which was for three arena facilities at three nights each).

Maintenance and Support for Special Events - Park managers told us that during the Park's tourist season, 70 percent of available maintenance hours are spent supporting special events. Park maintenance personnel are involved in preparing the facilities before a show, housekeeping and trash pickup during the show, and cleanup after the show. Park management, however, could not provide us with an accurate assessment of these costs because they have only recently begun to track them. Without an understanding of the varying maintenance costs associated with the numerous shows held at the Park, management cannot be sure it is recovering all the costs associated with the different events.

Contracting Procedures - We also found examples where the Park did not bill the contractually agreed-upon amount. For one event the billed amount excluded an

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\$85 telecommunications fee and charged \$100 less than was specified in the contract for each of two arenas. Though underpaid by \$285, the Park's contracting system did not note the discrepancy and marked the invoice for the event as paid.

Upon further investigation, we found that the accounting department does not routinely retain copies of the event contracts. We are concerned that this oversight to match contractually agreed upon rates to the amounts billed and paid indicates an underlying weakness in the Park's contracting system. Recommendation 1, at the end of this report, offers specific guidance on steps the Park can take to improve its cost accounting system.

Discount of Selected Events - Discounts are a form of expenditure by the Park in that they decrease revenue from event fees and admission. We found examples of rental fees at the Kentucky Horse Park which were not uniformly applied. For example, two events, lasting three days each, used facilities scheduled to rent for \$925.00 per day. However, the facilities were rented for only \$350.00 per day. These events also received stall rental discounts of \$4.00 per day. While these amounts may seem insignificant, for one of these events the stall rental discount alone represented over \$15,000 in lost revenue. For the two events combined, the total discount, including facility and stall rental discounts amounted to a total revenue loss of \$33,826.

Park management stated that other factors determine whether an event should be granted a discount from established fees. These factors include the economic impact of the event, indirect sales of admission tickets, concessions and gifts, and anticipated donations from event organizers. We believe that park subsidies and discounts must be identified, quantified, and appropriately reviewed in order to protect the taxpayer. Contractual arrangements should, when possible, detail the anticipated benefits the Park expects to receive in return for event discounts.

The State Fair Board, a similar state agency which also contracts with event organizers, has a policy requiring any contract that is not in accordance with established rental rates be submitted to the Fair Board for approval. Similarly, a recommended practice of the Government Finance Officers Association is to establish a formal policy which sets forth under what circumstances fees will be charged at less than the full cost of the provided services. We recommend that the Kentucky Horse Park Commission establish a policy with regard to such arrangements.

Possible Conflicts of Interest with Outside Entities Should Be Addressed

Increased public interest as well as recent statutory changes have brought new scrutiny to arrangements that might present a conflict of interest. Prudent business management, as well as generally accepted accounting and internal control standards, requires the establishment of policies to ensure compliance with laws and regulations and to reduce or eliminate conflicts of interest. We noted instances where the Commission and Park management can improve their current policies with regard to monitoring of potential conflicts of interest.

Ethics Commission Filing - Although he had not applied for approval from the Executive Branch Ethics Commission, the former Executive Director of the Kentucky Horse Park received a supplemental salary from the Kentucky Horse Park Foundation, in addition to his state salary of \$76,000. The supplemental salary, which totaled approximately \$26,000 in the last fiscal year, began in 1985 and was undertaken with the knowledge of officials in the Tourism Cabinet. However, in 1992, the Executive Branch Ethics Code was enacted as KRS Chapter 11A. KRS 11A.040, section 5, states, “No public servant shall knowingly accept compensation, other than that provided by law for public servants, for performance of his official duties without the prior approval of the commission.” In order to comply with State Ethics Guidelines, and to avoid the appearance of impropriety, the Kentucky Horse Park Executive Director should decline any unauthorized supplement to his state salary unless approved by the Ethics Commission. The current Executive Director has elected not to receive any supplemental salary from the Foundation.

Commission Members with Interests in Events - We noted that members of the Kentucky Horse Park Commission have, on occasion, financial interests in events and activities at the Park. Given that a portion of the members of the Commission are required by statute to be active in the horse industry, it is inevitable that such circumstances will occur. Furthermore, it may be impossible to avoid such circumstances since the Park’s purpose is to support and host the most prestigious industry events. While members of the Kentucky Horse Park Commission are not covered by the Executive Branch Ethics Regulations, the Commission has adopted a policy regarding disclosure of personal or private interests that may be in conflict with their status as a Commission member. We noted that with regard to the policy adopted by the Commission, members have disclosed their personal interests.

However, we believe it is essential to establish a more detailed Commission policy on how business arrangements should be conducted between the Park and individual Commission members acting in their own private interests. We believe the staff members of the Park may be placed in an awkward position when asked to negotiate contracts, discounts, and privileges for special events organized by Commission members who in turn are ultimately responsible for supervising and evaluating those same staff members. The policy should also include arrangements with the Kentucky Horse Park Foundation, since the Foundation membership includes nearly all of the Commission members. A review process, similar to the one at the State Fair Board, as discussed above, should also be established with regard to such activities.

Park Should Develop a Business Focus with Regard to Revenue Opportunities

Our audit also found that with improvements in contract management and cost accounting, the Park can improve its ability to maximize revenue. Given the successful attraction of events to the Park facility, the Commission and Park management should focus on increasing the level of revenue received by the Park. We are encouraged by the efforts already undertaken by the Commission to explore

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opportunities which focus on revenue generation. Through what has been named “Committee 2000”, members of the Kentucky Horse Park Commission and Foundation are working together to develop options for increasing the number of visitors to the Park through new investments, attractions, and marketing.

Senior managers of the Park stated that after the creation of the Kentucky Horse Park Commission in 1985, the management philosophy of the Park focused on attracting activities and events to the Park grounds. Furthermore, the Park was not necessarily expected to be self-sufficient and could justify its existence through the economic benefit it generated in the surrounding area. This philosophy focused on the Park’s role to, as called for in state statute, “advance and enhance the tourist industry, economy, entertainment, cultural, and educational interests of the public.” In fact, events at the Park have increased since the creation of the Commission. In 1978, the Park hosted its first major event. By 1989, the Park was hosting 34 events per year. The number increased to 41 in 1990, and for 1997, 67 events are scheduled at the Park. This increasing number of events has, in part, been responsible for the significant economic impact attributed to the Park.

We agree that any assessment of the Kentucky Horse Park must consider the full value of the Park, including intangibles such as enhancement of the state’s image.

We do not, however, believe that following more business-like, cost effective operating practices would diminish the educational or recreational mission of the Park.

In 1989, the ComPEL study of the Park asserted it was “...short-sighted to consider only direct revenues and expenses when measuring the impact of the Kentucky Horse Park.”³ The study went on to argue that the benefits the Park produced through tourism and enhancing the state’s image more than offset the Park’s revenue shortfalls. We agree that any assessment of the Kentucky Horse Park must consider the full value of the Park, including intangibles such as enhancement of the state’s image. According to the Cabinet for Tourism Development, the Kentucky Horse Park does provide a large amount of economic benefit to the surrounding area through direct and indirect expenditures, as well as by generating additional state and local tax revenue. We do not, however, believe that following more business-like, cost effective operating practices would diminish the educational or recreational mission of the Park.

As stated previously, legislation which established the Park (KRS 148.320) requires all revenues derived by the Commission to be used for the purpose of defraying the expenses of the Commission, the costs of managing and operating the Park, payment of debts incurred by the Commission, the development of adequate reserves for repair and replacement of facilities, as well as for expansions, additions and improvements to the facilities. It was the opinion of the Attorney General (80-399) that, by this statute, the Legislature did intend for the Park to be independent and self-sufficient.

While the Park may not be able to generate the level of revenue in the near future which would eliminate the need for general fund appropriations, the Kentucky Horse Park Commission and management should set clear short and long-term revenue goals which envision a self-sufficient Park. Currently, the management of the Park

³ ComPEL III, A Management and Accountability Study of the Kentucky Horse Park, December 1989, page 12; required by the 1988 General Assembly.

Does Kentucky Horse Park Management Ensure That Revenue Opportunities Appropriately Defray Park Expenses?

Such measures might include goals over the next five to ten years for attendance, revenue growth by type of event and Park patron, investment in Park facilities and new attractions, marketing efforts to attract visitors, and total General Fund support that will be needed.

relies on the biennial budget process as the main financial and performance planning exercise of the Park. Because the biennial budget focuses on the Park's immediate budgetary requirements, the establishment of long-term performance goals is essential to managing the dual goals of defraying Park expenses while providing economic and recreational benefits to the public. The Government Finance Officers Association (GFOA) lists the development of performance measures as a recommended practice in the area of budget and financial management. GFOA recommends that financial, service, and program performance measures be developed and used as an important component of decision making. Such measures might include goals over the next five to ten years for attendance, revenue growth by type of event and Park patron, investment in Park facilities and new attractions, marketing efforts to attract visitors, and total General Fund support that will be needed.

The Kentucky Horse Park Commission should also develop specific annual performance objectives for the staff of the Park. Per KRS 148.270 (2), "The executive director shall be the chief administrative officer and secretary of the commission and shall provide the staff direction and coordination in implementing the program and discharging the duties of the commission. The executive director shall serve as the administrative head of the Kentucky State Horse Park, thereby overseeing daily operations of the park." Since the Kentucky Horse Park Commission is not responsible for "daily operations of the park," it should clearly develop a set of expectations regarding Park efficiency and effectiveness.

Even if management wished to track costs as a tool for maximizing revenue, the Park has inadequate cost accounting information with which to conduct such analysis. Regarding the establishment of fees, GFOA recommends that the full cost of providing a service be calculated. The full cost includes direct and indirect costs, including operations and maintenance, overhead, and charges for the use of facilities. While plans have not been finalized for implementation of a cost accounting system, the Park has updated the computer hardware in its business office. Three outdated computers in the accounting office were replaced in the Fall of 1996 with four new networked Pentium computers.

As the Park undertakes opportunities to improve its business focus with regard to maximizing revenue, taking advantage of existing revenue sources and properly allocating costs, the Park can ensure that it does not require greater taxpayer subsidy than is necessary. We noted several opportunities in this report for the Park to maximize revenue. Other opportunities which Park management may wish to study include:

- using sales commissions to compensate gift shop and special event employees;
- more effectively controlling access to the Park grounds to increase revenue from parking and admission;
- revising the policy for establishing license fees and commissions from on-site vendors of feed, bedding, and other services; and
- marketing activities designed to attract visitors to the variety of events held at the Park.

We are concerned that, if revenue generation at the Park is not improved, the Park will have to request additional funding from the Legislature, delay necessary investment in and maintenance of Park facilities, or significantly curtail its services. Recently, in fact, the Park has requested \$800,000 in additional capital budget funding from the Legislature in order to build additional barns at the Park. Furthermore, the 1996-1998 Biennial Budget contains a request for an additional \$200,000 in capital outlays to fund equipment replacement which was deferred from the previous three years. We believe that through the recommendations noted below and the ongoing efforts of the Commission, revenue generated by the Park can play a larger role in offsetting these types of expenses, as envisioned by KRS 148.320.

Recommendations

We suggest that the Kentucky Horse Park Commission not be involved in day-to-day operations, but instead establish policies which delegate those decisions to the Executive Director of the Park and his professional management staff, who should base decisions on an analysis of the costs and benefits involved. KRS 148.270 (2) provides for the Executive Director to serve as the administrative head of the Park and oversee its daily operations. The Kentucky Horse Park Commission should concentrate on the overall performance of the Park and its director and on strategic planning decisions for the future. In order to improve operations and strengthen management oversight of Park activities, we have made the following specific recommendations.

Recommendation No. 1: We recommend that the Executive Director of the Kentucky Horse Park:

- 1.1 upon consultation with the Public Service Commission, determine the amount of debt service, operating, maintenance, and replacement costs which should be allocated to the waste water treatment center and recover the over \$22,000 of annual operating costs which are currently not being billed to entities inside and outside the Park grounds;
- 1.2 determine, invoice, and collect all amounts due from Park lessees for maintenance, sewer, and waste collection and removal;
- 1.3 enter into an annual contractual arrangement with the Kentucky Horse Park Foundation for the Southern Lights Exhibit which is based on a determination of the costs for maintenance, year-round storage, utilities, staffing, and other related operations incurred by the Park in order to support the exhibit and a determination of the suitable return for the rental of the Park's facilities and use of the Park's resources;
- 1.4 review all contractual obligations of the Park to ensure that clauses related to fees and maintenance are being enforced, including a careful review of all existing long-term contracts to ensure all agreed-upon fees are being collected;

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- 1.5 establish the business office as the repository for all signed contractual agreements of the Park;
- 1.6 establish a cost accounting system which allocates costs to individual facilities, activities, and events and estimates the revenues, expenses, and operating gain (or loss) from each event;
- 1.7 develop an annual revenue and expenditure budget by activity, service, and event, which shall be presented to the Kentucky Horse Park Commission for adoption.

The Kentucky Horse Park Commission, as a state agency, has the authority to enact by-laws and administrative regulations governing Park operations; to employ or contract with persons, firms, or corporations it deems necessary; and to fix the compensation and terms of employment of those with whom it has contracted. By establishing clear policies and performance objectives for Park staff, the Commission can effectively delegate operating decisions to the Executive Director and his staff while ensuring that its strategic direction regarding the future of the Park is maintained. The Commission also has exclusive control of concessions, exhibitions, shows, entertainment, and attractions at the Kentucky Horse Park. We believe the Park should strengthen its policies and procedures regarding contractual business relationships at the Park.

Recommendation No. 2: We recommend that the Kentucky Horse Park Commission:

- 2.1 establish and annually review short and long-term performance objectives for the Park and the Executive Director;
- 2.2 enter into written agreements with the Kentucky Horse Park Foundation for all transactions, including ongoing contractual obligations, transfers of assets, use of staff resources, and any other rights and obligations which may arise;
- 2.3 develop a policy statement which details how financial arrangements between the Commission (and Park) and the Foundation will be conducted;
- 2.4 develop a policy statement which details the procedures for Park facility usage when a member of the Commission has an interest in an event; and
- 2.5 establish formal procedures for the review of all contracts which are not in compliance with established rates as set by the Commission. Such review should include the Secretary of Tourism Development or his/her representative and the review of each contract should be noted as part of

Does Kentucky Horse Park Management Ensure That Revenue Opportunities Appropriately Defray Park Expenses?

the official record of the Commission.

In light of the broad powers allocated to the Kentucky Horse Park Commission, and the Commission's dual mandate to serve both the equine industry and the state, we feel the state must exercise its budgetary authority over the Park to protect the state's considerable investment in the Park. Park subsidies for events or activities must be identified, quantified, and appropriately limited to protect the taxpayer. Since the Park is a budgetary unit of the Tourism Development Cabinet, and in light of the Secretary of the Tourism Development Cabinet's responsibility to approve, disapprove, modify, or otherwise amend the budget request of any Cabinet budgetary units or administrative bodies, we believe oversight authority for the Park resides with the Secretary of Tourism Development.

Recommendation No. 3: We recommend that the Secretary of the Tourism Development Cabinet:

- 3.1 annually review and approve the Park's fee structure; and
- 3.2 review and offer comments on the annual revenue and expenditure budget by activity, service, and event as approved by the Kentucky Horse Park Commission.

**Response to Agency
Comments**

Horse Park management has expressed concern that if they raise prices to increase revenue, they will drive events away and reduce the overall economic benefit of the Park. We acknowledge a challenging dual responsibility for Park management. We also note that virtually every weekend throughout the Horse Park's tourist season is scheduled. In fact, the Park has been forced to turn away \$200,000 worth of business for 1997 because facilities were already scheduled.

Park management also stated that the establishment of fees at the Park is based on a survey of rates charged at similar facilities. We feel it is important to note that the Kentucky Horse Park is a unique facility which may demand an above average fee. Furthermore, analyzing revenue and expenditures by event will allow Park management to select among competing events. With such a strong demand for the facilities available at the Kentucky Horse Park, management should be able to recover a greater portion of the costs of providing these facilities. To do otherwise would constitute an unnecessary taxpayer subsidy for the events held at the Park.

We are pleased that Park management acknowledges its responsibility to have written contractual agreements for the Southern Lights Event. Park management wished to emphasize the large attendance this event brings to the Park in the winter, current donations as a result of the Foundation proceeds, and expected future returns to the Park. While we did acknowledge these points in our report, our recommendation addresses our concern that without a long-term written agreement, the Park cannot be assured of these proceeds. Again, we emphasize, all relationships with outside entities should be by contractual agreements.

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With regard to all events which receive discounts, Park management wished to emphasize the value many of these events provide to the Park or Kentucky Horse Park Foundation. While the Park should certainly continue to offer discounts to selected events, our recommendation reflects our belief that such arrangements should be appropriately justified and documented.

With regard to the billing of waste water treatment facility user fees, Park Management noted their previous efforts to determine who regulates the facility and what charges are appropriate. Although the Public Service Commission (PSC) has yet to make an official determination regarding its oversight jurisdiction, the report accurately reflects our interviews with PSC staff. One Finance and Administration official also indicated that the Park had been advised in the past to charge the full cost of treatment services to all respective users. Our key point remains the same, the PSC has a competency in rate setting that should be used by the KHP regardless of whether the PSC has a regulatory oversight rule of the Park's treatment facility. We believe the various agencies should cooperate and resolve this issue immediately so that the Park no longer subsidizes other state agencies and private organizations.

Management of the Kentucky Horse Park has agreed with the recommendations contained in this report. An implementation team has already been established and is working to address the concerns we have noted. Appendix III contains the complete text of the Agency's formal comments.

Scope

We performed our audit in accordance with generally accepted government auditing standards, primarily at the Kentucky Horse Park, to develop recommendations and information useful in assisting management in developing efficient business practices. Field work was conducted between January, 1997, and May, 1997.

We did not independently validate the Kentucky Cabinet for Tourism Development analysis of the economic impact of the Kentucky Horse Park. We further relied, without verification, on the published reports of the Lexington Chamber of Commerce ComPEL III study and the published Financial Statements of the Kentucky Horse Park audited by Independent Public Accountants. Our review of the Kentucky Horse Park Foundation, a private organization, was limited to the Foundation's published financial statements and that information which was made available by the staff of the Kentucky Horse Park..

Methodology

In order to obtain an understanding of the origin and mission of the Kentucky Horse Park, we reviewed legislation and statutes relevant to the creation and organization of the Park, as well as the relevant Opinions of the Attorney General. We also reviewed past audit reports for the Park performed by the Auditor of Public Accounts and independent public accounting firms.

In order to obtain an understanding of the management controls, we interviewed management personnel from operating divisions within the Park, as well as personnel from the Kentucky Horse Park Commission and Foundation. Additionally, we obtained and reviewed the following information:

- Kentucky Horse Park Master Plan.
- Kentucky Horse Park Commission meeting minutes for calendar year 1996.
- KHP Annual Financial Report.
- KHP Media Expenditures FY 96/97.
- A Marketing Proposal for KHP FY 96/97.
- ComPEL III - A Management and Accountability Study of the Kentucky Horse Park.
- Kentucky - Tourism Master Plan - Fall 1995.
- The Economic Impact of the Horse Industry in the United States - National Summary December 9, 1996.

We also analyzed Kentucky Horse Park cost and revenue information, as well as economic data and analyses generated by the Kentucky Cabinet for Tourism Development. We reviewed contractual information relating to the annual Southern Lights display, as well as contractual agreements for the leasing of office space in four buildings at the Park; several special events facility rental contracts and related approved fee schedules; several show bills provided by promoters; audit reports for KHP Foundation for the year ended May 31, 1995, and 1996; and the by-laws and annual budget of the KHP Foundation as of May 31, 1996. We also contacted other large facilities hosting similar events in order to obtain relevant comparable evidence for our audit.

Recommendations From The ComPEL III Study On The Kentucky Horse Park

Conducted by the Lexington Chamber of Commerce, the ComPEL III study looked at operations of the Park in 1989. The following recommendations were included in that study.

- Institute a computer information system as a means for reliable and timely financial management information.
- Develop a new monthly-basis financial management report to include: a) monthly revenue/expense comparisons to the budget on a line-item basis, with explanations denoting deviations where present; and b) data segregated to indicate gross profit or loss generated from areas of the Park that produce their own revenue and expenses (e.g., campground, gift shop).
- Follow through immediately on recommendations of the Commonwealth's Auditor of Public Accounts relating to internal accounting procedures.
- Immediately establish more effective control of revenues relating to admissions, parking and merchandise inventory.
- Complete a long-term goal of establishing an in-park network of intelligent terminals (PCs) connected to a central processor to provide for more sophisticated operations along with better access to data in the Park and in Frankfort.
- Computerize six management functions (Park Administration, Retail, Maintenance, Reservations, Exhibits, Equine Management) so as to yield immediate benefits for better management control of information.
- Develop additional equine attractions at the Park that are compatible with the theme and personality of the Park.
- Draw tourist attention to the unrivaled museum by making it an integral part of the official name for the facility (i.e., "Kentucky Horse Park & Museum").
- Allocate more funds for marketing purposes, or appropriate additional funds from state coffers explicitly for such purposes.
- Re-evaluate and redefine markets, public and trade segments for advertising campaigns.
- Define and establish realistic marketing goals that can be accomplished with increased resources that are made available. Identify and select segments of the Horse Park that have the greatest potential for development and growth. Focus the greatest share of these resources on those activities or areas.
- Establish a goal of moderate growth in admissions of ten percent per year compounded over the next five years, and determine what would be required to achieve dramatic growth in admissions of 20 percent per year to increase visitors from 400,000 towards one million. Develop a strategy and determine the required resources to achieve the five-year plan goal.
- Develop broad-based, aggressive, proactive publicity campaigns aimed at all levels of potential visitors—local, state, regional, and national.
- Use exit surveys and visitor comment cards for gathering valuable research data on the demographic, geographic and psychographic traits of the Park patrons.
- Establish better coordination and/or integration of advertising media plans and consolidate spending among the Horse Park, Travel Development Department and Lexington Convention & Visitors Bureau.
- Offer selective horse farm tours emanating from the Horse Park.
- Further develop and promote additional special events that would bring national attention to the Park.
- Develop official sponsorship programs through major national corporations to generate additional revenues or free-up existing resources for enhanced marketing efforts.

- Pursue Computer Information Systems' recommendation for proper scheduling of maintenance activity of grounds, personnel, and equipment.
- Investigate further several options for operation of the wastewater treatment facility—
a) construction of a line to tie into the Lexington-Fayette Urban County Government sanitary sewer system (costs should be shared with other state agencies near Spindletop); b) contracting with a private firm to operate and maintain the plant (costs should be shared with other state agencies).
- Prepare a cost/benefit analysis of the equipment lease program. Give consideration to increasing the equipment maintenance capabilities by hiring a trained mechanic, upgrading the service area and maintaining a supply inventory of frequently-used parts.
- Conduct a cost/benefit analysis of garbage collection by an outside contractor.
- Initiate capital budgeting for clean-up, repair and beautification of the lake including widening of the road across the "dam".
- Ensure that the Foundation remains a supplement, not an alternative, to the Commonwealth's funding of the Park and Museum. Also, fiscal operations of the Horse Park, the Horse Park Commission and the Foundation should remain totally segregated.
- Gear fund-raising efforts by the Foundation toward specific improvements or acquisition projects defined as a priority or need. The Foundation should also act as the catalyst for major gifts and development projects similar to equipment promotions such as those with Toyota and Wheel Horse.
- Consider targeting special equine interest groups and businesses that have a potential for monetary and in-kind support as part of the fund-raising efforts.
- Continue to have the Foundation give consideration to the recommendations of its consultants as opportunities for the Foundation change in the future.
- Continue the personal involvement of the governor in the efforts to bring equine associations to the Bluegrass. A task force should be appointed to study the development constraints for additional facilities at the National Horse Center, as well as the feasibility of "spec" building.
- Encourage the Cabinet for Economic Development to become more actively involved in the efforts to entice relocation of equine associations to the Commonwealth. Also, for-profit equine-related businesses should be targeted by economic development marketing offices on the state and local level.

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PAUL E. PATTON, Governor
ANN R. LATTI, Secretary
DAVID LOVELACE, Deputy Secretary

June 24, 1997
Official Comment from Ann Latta,
Secretary, Tourism Development Cabinet

In Re: Performance Audit of the Kentucky Horse Park
Prepared by Edward B. Hatchett Jr.,
Auditor of Public Accounts

Upon examination of the Audit of Revenue Management Practices at the Kentucky Horse Park, I congratulate the Kentucky Auditor's office for a thorough and in-depth analysis of the park's management processes. Undertaken as a "Performance Audit", it is and should be perceived as, a management tool to help guide the park's staff and the Horse Park Commission, which is the administering agency attached to the Tourism Development Cabinet. I concur with the specific recommendations as regards oversight of park operations by the Tourism Development Cabinet, and will ensure that these recommendations are carried out.

As the Audit rightly notes, the park has faced various challenges over its 20-year history. From its inception, there have been constant struggles to bring it to the position it occupies today as a world-renowned showcase for Kentucky's most famous symbol: the horse. Those who have guided the park's destiny and made valuable contributions to its operations over the years have always had foremost as their goal, the creation of a facility which would bring pride to Kentuckians and to horse lovers everywhere. That this goal has been achieved is recognition of their efforts.

The Horse Park's economic value to the Commonwealth can be recognized by virtue of the nearly \$10 million in state and local taxes generated by its operations. These tax dollars provide a source for the approximately \$2 million per year in general fund appropriations to the park for debt service and operations. Strengthening the park's management practices, as recommended in the Performance Audit, could reduce some reliance on general fund support and must be pursued. But in this context, the park's mission to advance Kentucky's horse industry must also be given consideration. That role necessitates many non-revenue-producing activities, including maintenance and grounds-keeping. Capital expenditures additionally might not be expected to decrease in the future, but to keep pace with the park's age and growth.

An Equal Opportunity Employer

The Kentucky Horse Park Education Foundation, as noted in the Performance Audit, has contributed more than \$6 million to the park in cash and kind since its inception in 1985. Clearly much of the park's success must be attributed to the generosity and dedication of this group. The Tourism Development Cabinet recognizes the Foundation's efforts and supports any procedures for strengthening the relationship between the Foundation and the Horse Park.

In 1998 the Horse Park celebrates its 20th year of operations. Having achieved stature in the horse world and success as a major tourist attraction for Kentucky through outward-directed activities, it is appropriate at this time to re-examine internal operations. The Commission recognized this need when it initiated the "Committee 2000" study earlier this year. Park management, relying on outdated computer equipment until just last fall, is already examining and strengthening the business operations. The Cabinet Secretary will benefit from more in-depth reports when preparing and submitting budget requests. In all of these activities, the Performance Audit will provide useful guidelines to enable the park to fulfill its total mission to the citizens of Kentucky.

**KENTUCKY HORSE PARK**

4089 Iron Works Pike Lexington, Kentucky 40511 (606) 233-4303

PAUL E. PATTON
GOVERNORANN LATTI
SECRETARY, TOURISM CABINETJohn Nicholson
EXECUTIVE DIRECTOR

June 18, 1997

Edward B. Hatchett, Jr.
Auditor of Public Accounts
144 Capital Annex
Frankfort, KY 40601

Dear Mr. Hatchett,

The management of the Kentucky Horse Park has thoroughly reviewed the findings and recommendations of the audit of revenue management that have been presented to the Kentucky Horse Park Commission on this date. The tireless efforts of the audit team and other members of your staff are recognized and appreciated. We are pleased to inform you that we believe much of the substance of the audit to be valuable and highly useful. In view of the fact that I have only recently been appointed as Executive Director, you can be assured that this audit will be an operative and ever present document as I outline the administrative agenda for this special and wonderfully unique equine facility.


Park management concurs with all of the specific recommendations contained in Recommendation No. 1, which is directed singularly to the Executive Director. As you have stated in your introductory letter, steps have already been taken to implement recommendation 1.5 regarding the maintenance of contracts and, therefore this recommendation is considered closed. It is my intention to form a task force within Park management to implement the other recommendations as quickly as possible.

We are also most appreciative of the acknowledgment in your report that management has created an acclaimed attraction that hosts world class equine events, attracts tourism and creates a positive economic impact on the community. This recognition of the Horse Park's success only serves to increase our resolve to institute those procedures which can allow us to enhance the positive reputation the Horse Park now enjoys. We are also most pleased that your audit team stated that they were encouraged by the dedication of the Park staff and the innovation involved in the development of plans underway for the Park. I can attest that this is typical of a standard of excellence long in place at the Kentucky Horse Park.

As stated, Park management accepts and will implement all the specific recommendations outlined in Recommendation No. 1. There are, however, certain assumptions, statements and conclusions that are contained in the report that management believes to be less than accurate, incomplete, or at least deserving of clarification.

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We believe, for example, that it should be understood by all involved or interested that the Horse Park has for a number of years, through various administrations, been seeking guidance regarding the entire issue of the Park's Waste Water Treatment Facility. We concur with the sense of urgency implied by the audit. The Park's experience, however, would strongly indicate that the report's assumption that the Public Service Commission is the governing agency is the subject of much divergent opinion. In fact, the Park's previous consultation with the Commissioner of Facilities Management specifically indicated that the PSC did not have authority over the Waste Water Treatment Facility. The Kentucky Horse Park will continue its efforts to obtain effective assistance regarding this complicated issue. The report, in the view of management, should have clearly stated the Park's sincere efforts to resolve this issue and to collect those fees that most agree are due the Park. We acknowledge with appreciation that the report noted that, despite difficulties surrounding this facility, the Park exceeds Kentucky Division of Water treatment standards.

The Kentucky Horse Park will, as recommended in the report, enter into a contractual agreement with the Kentucky Horse Park Foundation for the 1997 and all subsequent Southern Lights. We agree that, although there was a written agreement outlined between the two entities at the inception of the event, there should be a new agreement signed annually.

We believe fairness dictates that the report should not have omitted the fact that the Foundation borrowed the initial investment to purchase the lights from a lending institution and this loan was to be retired first and then there would be a significant increase in the direct revenue received by the Park. This was the long term understanding between the Park and the organizers. This point should be recalled when examining the comparative revenue divided between the Horse Park, the KHP Foundation and the Lexington Herald-Leader. Again, we agree that comprehensive written agreements are always the best policy in these types of relationships.

Park management would also note that Southern Lights is an evening event. The Park charges neither a parking nor admission fee after 5:00 p.m. In fact, during the winter months, the Park does not charge a parking fee at any time during the day. In view of these facts, any statement indicating lost admission and parking revenue due to Southern Lights is of little value.

More importantly, the report seems to place little emphasis on the importance of attracting new visitors to the Park at a time of the year when there are traditionally few visitors to the Park. This is not an ancillary point - it is a fundamental part of the Park's reasoning in committing to this event. Management also believes that the report should have acknowledged and quantified the vast amount of free advertising given to the Park as a result of its participation in the partnership.

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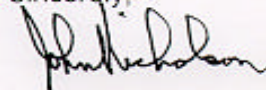
As previously stated, the Kentucky Horse Park concurs without reservation to the recommendation regarding having a contractual agreement with the KHP Foundation for Southern Lights. We believe the commentary that accompanies this recommendation is incomplete, much too narrow in scope and is not an accurate reflection of what management believes is a great event for the Horse Park and the community as a whole.

Park management is particularly enthusiastic regarding plans to implement a program of cost analysis for its events and other forms of programming. We agree that a system of cost analysis will prove to be an excellent managerial tool in the evaluation of current and future events and programming. In the midst of this enthusiasm, however, we believe that we should remain mindful that cost accounting should not be the only factor in making managerial determinations regarding events. Other vitally important factors should be included such as, but not limited to, economic impact, prestige, cultural benefit and longevity. As long as the concept of cost accounting is placed in this context, then it plays an effective role in the decision making process.

An example of the danger of relying solely on cost information to make pricing decisions is reflected in the report's discussion of stall fees. It is inaccurate to state that the staff recommended a \$3.30 per night increase in stall fees. An individual staff member prepared an analysis of the cost per day of muck removal. It was not a recommendation to increase the fees. The Commission, after much debate, and after considering all factors, including market forces, decided that it was best to institute a \$1.00 per night increase for the first year and then examine the effect before deciding to institute further increases. Again, fairness dictates a more thorough examination of all the factors that may have entered into the Commission's collective action.

The Kentucky Horse Park will celebrate its twentieth anniversary in 1998. Any objective historical analysis of the Park can only conclude that, by almost any measure, it is one of the great success stories of the Commonwealth of Kentucky. We will implement the recommendations of this audit so that we will be better able to continue to grow and to manage the Horse Park's remarkable success.

Sincerely,



John Nicholson
Executive Director

**KENTUCKY HORSE PARK**

4089 Iron Works Pike Lexington, Kentucky 40511 (606) 233-4303

PAUL E. PATTON
GOVERNORANN LATTA
SECRETARY, TOURISM CABINETJohn Nicholson
EXECUTIVE DIRECTOR

June 23, 1997

**OFFICIAL COMMENT FROM CORNELIA BONNIE
CHAIR, KENTUCKY HORSE PARK COMMISSION**

In Re: Performance Audit Of The Kentucky Horse Park
Prepared By Edward B. Hatchett, Jr.,
Auditor Of Public Accounts

The Official Comment from Ann Latta, Secretary, Tourism Development Cabinet, which has been made a part of this Audit, accurately reflects the feelings of the Kentucky Horse Park Commission, and we unanimously endorse it. The only purpose of my comment is to expand on the factual background of certain items discussed in the Audit so that a complete understanding may be had relative to those items.

1. SOUTHERN LIGHTS.

As the Audit points out, the Kentucky Horse Park Foundation and the Lexington Herald-Leader, Inc. entered into a Joint Venture Agreement to create an annual Christmas light show called "Southern Lights," to be held at the Kentucky Horse Park. The concept of Southern Lights is to utilize the Park during the "slow season" by creating revenue which would not normally be available, and to promote Kentucky and the Lexington community with a nationally known first-class light show and entertainment during the Holiday Season.

The start-up costs (purchase of lights, etc.) and the cost of additional lights over the last three years total approximately \$500,000.00, and all of the revenue received by the joint venture in 1994 and 1995 was applied toward paying off these costs. 1996 was the first year that "Southern Lights" realized a profit, with \$50,000.00 going to the Lexington Herald-Leader, Inc.'s charitable foundation and \$50,000.00 to the Kentucky Horse Park Foundation. The Lexington Herald-Leader, Inc. donated \$25,000.00 to the Calumet Trophy Fund and \$25,000.00 to Kentucky food relief. The Kentucky Horse Park Foundation has spent \$20,000.00 of its share for a mobile gift shop for the Park and is discussing with park management how to spend the other \$30,000.00.

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It is important to note that all monies raised by the Kentucky Horse Park Foundation are spent on the improvement of the Kentucky Horse Park. In addition, the Lexington Herald-Leader provides over \$100,000.00 of donated advertising for Southern Lights each year.

2. DISCOUNT OF SELECTED EVENTS.

Park management sometimes agrees to a discount on certain fees for a specific event after considering various factors including the economic impact of the particular event or some other benefit which will be returned to the Park because the event is held there. The two events specifically referred to in the Audit have received the discounts set forth. However, in return for receiving the discounts, the two sponsors agreed to return forty (40%) percent and sixty (60%) percent of the profits, respectively, made on the events to the Kentucky Horse Park Foundation, which in turn spends that money for the benefit of the Park.

Over the past ten (10) years during which those two events have been held at the Park, profits donated to the Kentucky Horse Park Foundation total over \$343,000.00. In addition, individual contributions to the Foundation generated from people connected with said events have totaled over \$102,000.00.

Therefore, by attracting these two events to the Horse Park by negotiating discounts, the Horse Park has received over \$445,000.00 which has funded the majority of improvements that make the show complex one of the finest in America and very desirable to major shows. These improvements include one hundred stalls, eight all-weather rings and schooling areas, roads, landscaping, a pavilion, other show-related buildings and highly improved lighting in the indoor arena. The Audit correctly points out that each such event should be analyzed periodically to make sure that the Park is receiving a sufficient benefit, whether monetary or intangible, to justify any discounts.

Because of the hard work and devotion of many people over the past twenty (20) years, the Kentucky Horse Park today is a world-class and world-renowned facility. It will take that same hard work and devotion over the next twenty (20) years for the Kentucky Horse Park to maintain and enhance that reputation. This Audit will provide us tools which will be helpful in that effort.

Contributors To This Report

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General Questions

General questions should be directed to Donna Dixon, Intergovernmental Liaison, or Ed Lynch, Director of Communications. They may be reached at (502) 564-5841 or at the APA address listed above.